



RATING ACTION COMMENTARY

Fitch Rates State of Washington's \$1.3B GOs 'AA+'; Outlook Stable

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Fitch Ratings - New York - 15 Apr 2022: Fitch Ratings has assigned a 'AA+' rating to the following State of Washington general obligation (GO) bonds:

--\$831,240,000 various purpose GO refunding bonds, series R-2022C;

--\$497,825,000 MVFT GO refunding bonds, series R-2022D.

In addition, Fitch has affirmed the state's 'AA+' Issuer Default Rating (IDR), the 'AA+' rating on the state's outstanding GO bonds and the Washington school district credit enhancement program (School Bond Guarantee or SBG program) at 'AA+'.

The Rating Outlook is Stable.

The series R-2022C and D bonds are expected to sell competitively on or about April 26. The proceeds of the bonds will be primarily to refund certain outstanding GO bonds. Par amounts are subject to change.

SECURITY

All GO bonds are general obligations of the state to which the state has irrevocably pledged its full faith, credit and taxing power.

ANALYTICAL CONCLUSION

Washington's 'AA+' IDR and GO bond rating reflect the state's broad and steadily growing economy, with solid long-term revenue growth prospects, a demonstrated commitment to fiscal balance and combined long-term liabilities that place a low burden on resources. The ratings also reflect the state's very strong financial resilience supported by a statutory requirement for a balanced multiyear budget and formulaic funding of the budget stabilization account (BSA) leading to solid reserves. Education poses a unique spending pressure for the state given both steady population growth and the state's role as the primary funder for K-12 schools across the state.

Economic Resource Base

Washington's fundamental economic profile remains strong, with steady growth, particularly in information-technology, and a diverse employment base. Income levels are above the national average and high educational attainment also supports continued economic gains.

KEY RATING DRIVERS

Revenue Framework: 'aaa'

Revenue performance over time has generally been above inflation, and Fitch expects this to continue to support solid growth prospects. The state has complete independent control over taxation, with an unlimited legal ability to raise operating revenues as needed.

Expenditure Framework: 'aa'

Washington benefits from solid expenditure flexibility, although its flexibility is somewhat more restricted than most states due to court mandates, statutory commitments and broad responsibility for education funding. Rapid demographic growth also exerts pressure on infrastructure spending. The state has a low burden of carrying costs and benefits from the broad expense-cutting authority common to most U.S. states.

Long-Term Liability Burden: 'aaa'

The combined burden of debt plus pensions is low as a percentage of personal income but above the median for U.S. states. Elevated debt ratios incorporate the funding of

substantial capital needs, particularly for transportation, but are offset by a moderate net pension liability and an expanding economic resource base.

Operating Performance: 'aa'

Washington maintains very strong gap-closing capacity in the form of its superior budget flexibility and solid reserves. The state has prudently built up reserves in times of economic recovery and expansion, despite spending pressure for education and other pressing needs.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to a positive rating action/upgrade:

- Strong economic and revenue growth that outpaces national GDP over time;
- Demonstrating the highest level of operating performance through the current economic recovery by managing higher spending for education and overall growth pressures, while establishing superior gap-closing capacity, such as through building reserves towards the recent peak of 20% of spending.

Factors that could, individually or collectively, lead to a negative rating action/downgrade:

- A sustained increase in the long-term liability burden to 10% or more of personal income;
- Unanticipated shift in fiscal management that materially weakens fiscal resilience, such as sizable and continuing draws on reserves to support operations, particularly during times of economic expansion.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit

<https://www.fitchratings.com/site/re/10111579>.

CURRENT DEVELOPMENTS

Economic Recovery Picks Up Pace

Washington's recovery from the pandemic has been in line with national trends. As of February 2022, the state had recovered 89% of jobs lost in the first months of the pandemic, consistent with the 90% national recovery. Washington had been lagging national trends, but the pace of jobs growth accelerated at a faster rate in the second half of 2021 and into 2022. Headline unemployment of 4.3% in February was slightly above the national 3.8% rate that month, consistent with the pattern heading into the pandemic. Washington's labor force growth has been ahead of national trends, reflecting the state's ongoing economic expansion.

Washington Fiscal Update

Improving economic conditions and conservative initial forecasts have supported increases in the state's official revenue forecasts with four upward revisions over the past year. The most recent update from the state's Economic and Revenue Forecast Council (ERFC) in February projected fiscal 2022 and 2023 revenues at \$5 billion more than the enacted budget for the 2021-2023 biennium. The ERFC primarily raised their outlook for the sales and use tax, the state's primary broad-based tax, and the business and occupations tax (B&O, a gross receipts tax levied on businesses). The council also made a notable upward revision to the real estate excise tax, reflecting the robust housing and commercial markets. Better-than-expected revenue performance continues a trend the state has experienced since soon after the pandemic's onset, primarily driven by the vast federal economic stimulus provided since March 2020.

Supported by the increased revenue forecast, as well as federal receipts from the American Rescue Plan Act (ARPA), the state enacted a supplemental 2022 budget bill last month that adds another approximately \$5 billion in near general fund (NGF) appropriations for the current biennium. NGF is the designation for the state's primary operating funds. The additional appropriations are a mix of one-time allocations such as \$2 billion transfer to the state's transportation fund and most of the \$1.1 billion of allocated ARPA aid and recurring spending such as \$232 million for wage and compensation increases for state employees.

The state's budgetary reserves have shifted considerably through the pandemic and are now on a path towards restoring pre-pandemic levels. Reduced balances in the constitutional budget stabilization account (BSA) were followed by a sharp increase in ending balance and now a projected decline as surplus revenues are appropriated as noted

above in the supplemental 2022 budget bill noted earlier. The legislature also established a new reserve fund, the Washington Rescue Plan Transition Account (WRPTA) and allocated \$1 billion towards it in fiscal 2022 in the enacted biennial budget. The supplemental 2022 budget bill adds another \$1.2 billion next fiscal year. The WRPTA has statutory restrictions, but they are relatively broad and the fund provides an important source of future fiscal flexibility for Washington.

In the current Four-Year Budget Outlook (a statutorily-required budget forecast that reflects the supplemental 2022 budget bill), the state anticipates another \$500 million WRPTA deposit in fiscal 2025. By the end of the 2023-2025 biennium, the budget outlook forecasts combined reserves (ending balance plus BSA plus WRPTA) of \$4.2 billion or nearly 13% of projected revenues and other resources. This compares to \$6.5 billion at the end of this fiscal year before full effect of the supplemental budget bill, and a pre-pandemic peak of \$3.6 billion at the end of fiscal 2019.

CREDIT PROFILE

School Bond Guarantee Program Details

The 'AA+' rating on the school credit enhancement program, or SBG, reflects Washington's full faith, credit and taxing power pledge to guarantee full and timely payment of principal and interest on the debt of participating school districts. As of April 1, 2022, the aggregate total principal amount outstanding on 461 voter-approved bond issues guaranteed under the program was \$16 billion. The bonds were issued by 170 school districts.

The program has both constitutional and statutory basis in state law including Article VIII, Section 1 (e) of the state constitution and the Revised Code of Washington, Title 39, Chapter 98. The statute also outlines the mechanics of the state's GO guarantee. County treasurers collect property taxes used for debt service, paying them paying agents. The school district, the county treasurer and the paying agent all bear responsibility for contacting the state treasurer in the event of a shortfall.

Notification requirements provide sufficient time for the state treasurer to forward payments to the paying agent prior to debt service due dates. The authorizing statute provides that the state legislature must appropriate, in each and every biennial appropriations act, the amount needed to make timely payment on any SBG Bonds. For fiscal 2022, the state estimates total debt service on SBG Program bonds of \$1.6 billion. The state's backstop is not linked to or limited by state aid distributions due to any particular school district.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit

www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT ⇅	RATING ⇅			PRIOR ⇅
Washington, State of (WA) [General Government]	LT IDR	AA+ Rating Outlook Stable		AA+ Rating Outlook Stable
	Affirmed			
Washington School District Credit Enhancement Program (WA) /State School Bond Program Rating/1 LT	LT	AA+ Rating Outlook Stable	Affirmed	AA+ Rating Outlook Stable
Washington, State of (WA) /General Obligation - Unlimited Tax/1 LT	LT	AA+ Rating Outlook Stable	Affirmed	AA+ Rating Outlook Stable

[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

U.S. Public Finance Tax-Supported Rating Criteria (pub. 04 May 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 ([1](#))

ADDITIONAL DISCLOSURES

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ENDORSEMENT STATUS

Washington School District Credit Enhancement Program (WA)

EU Endorsed, UK Endorsed



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